GINLON (M) SDN BHD

v.

MBF FINANCE BHD

COURT OF APPEAL, KUALA LUMPUR
MOKHTAR SIDIN JCA
ABDUL KADIR SULAIMAN JCA
ABDUL AZIZ MOHAMAD JCA
[CIVIL APPEAL NO: W-02-436-1997]
4 MARCH 2004

LAND LAW: *Charge - Validity of - Land charged as security for loan - Whether there was a variation in loan agreement without chargor's consent to render charge null and void by virtue of s. 86 Contracts Act 1950 - Whether s. 86 pertains to discharge of surety and not invalidation of charge*

CONTRACT: *Surety - Discharge of surety by variance in terms of contract - Section 86 Contracts Act 1950 - Whether also applies to render charge on land null and void - Whether s. 86 pertains to discharge of surety and not invalidation of charge*

By a letter of offer, the respondent, a licensed finance company, agreed to grant a loan of RM300,000 to a company called Pembinaan Ikhlas-Jae Sdn Bhd ('the borrower'). Among the securities specified in the letter of offer were a charge on the appellant's land and an assignment ('the assignment') to the respondent of payments due to the borrower from a project by one MBf Construction Sdn Bhd. When the loan agreement was duly executed between the borrower and the respondent, the loan was for RM250,000 and not RM300,000. The loan agreement also did not specify the assignment as one of the securities for the loan. Subsequently, the borrower sought from the respondent a waiver of the assignment as security on the ground that MBf Construction Sdn Bhd refused consent to the assignment. The respondent agreed to the said waiver and that the loan amount was reduced from RM300,000 to RM250,000 due to insufficient security coverage. Subsequently the loan sum of RM250,000 was disbursed. Upon default of the loan, the respondent sought to enforce the charge by applying to the Land Office for an order for sale. The appellant then commenced an action in the High Court for a declaration that the charge was null and void by virtue of s. 86 of the Contracts Act 1950 ('the Act'). The appellant submitted that there was a variance in the loan agreement as there was a waiver of the assignment. The learned judge dismissed the action. Hence, the appellant's appeal.

Held:
Per Abdul Aziz Mohamad JCA

[1] There was no variance in the terms of the loan agreement as regards the assignment as it was never in the agreement in the first place. The question of s. 86 of the Act could not even begin to arise. Even if the loan agreement had contained the term as to the assignment and subsequently the term was removed without the consent of the appellants, s. 86 would still not apply. Section 86 was not intended to effect a charge. The consequence of s. 86 was the discharge of the surety and not the invalidation of a charge. (p 174 a-b)

[2] Under s. 79 of the Act, a surety under a contract of guarantee performs the promise, or discharges the liability of a third person in case of his default. The remedy of the person to whom the guarantee is given is therefore to sue the surety on his undertaking in the contract of guarantee if the third person defaults. By the charge, the chargor does not guarantee to perform the promise or discharge the liability of a third person in case of his default. The remedy under the charge is not against the person of the chargor but against the property charged, ie, the remedy of sale or taking possession of the property. A charge is not a contract of guarantee and the chargor is not a surety. A charge is a statutory instrument, a dealing that the Code authorizes. Therefore, in the present case even if there was a variance of the loan agreement by the waiver of the assignment and the variance was made without the appellant's consent, s. 86 did not apply to render the charge void in consequence. (p 174 c-h)

[Appeal dismissed.]

*[**Bahasa Malaysia** Translation Of Headnotes*

Melalui satu surat tawaran, responden, sebuah syarikat kewangan berlesen, bersetuju untuk memberikan pinjaman berjumlah RM300,000 kepada syarikat yang bernama Pembinaan Ikhlas-Jae Sdn Bhd ('peminjam'). Antara cagaran yang dinyatakan dalam surat tawaran adalah gadaian tanah perayu kepada responden dan serahanhak ('serahanhak') kepada responden akan bayaran-bayaran yang dibayar kepada peminjam berkaitan satu projek oleh MBf Construction Sdn Bhd. Apabila perjanjian pinjaman dimeterai oleh peminjam dan responden, pinjaman bagaimanapun adalah untuk jumlah RM250,000 dan bukannya RM300,000. Selain itu, perjanjian pinjaman juga tidak menyenaraikan serahanhak sebagai salah satu cagaran kepada pinjaman. Kemudian daripada itu peminjam memohon kepada responden supaya melepaskan serahanhak dari menjadi jaminan kepada pinjaman atas alasan bahawa MBf Construction enggan

memberi izin untuk serahanhak tersebut. Responden bersetuju kepada pelepasan dan pinjaman dikurangkan dari RM300,000 kepada RM250,000 disebabkan jaminan yang tidak mencukupi. Berikutnya, pinjaman sebanyak RM250,000 telah dikeluarkan. Apabila berlaku kemungkiran ke atas pinjaman, responden cuba melaksanakan gadaian dengan cara memohon kepada Pejabat Tanah untuk perintah jualan. Perayu membalas dengan memulakan tindakan di Mahkamah Tinggi bagi mendapatkan perisytiharan bahawa gadaian adalah batal dan tak sah berdasarkan s. 86 Akta Kontrak 1950 ('Akta'). Perayu berhujah bahawa terdapat perselisihan pada perjanjian pinjaman yang disebabkan oleh pelepasan serahanhak. Yang arif hakim menolak permohonan dan perayu merayu.

Diputuskan:
Oleh Abdul Aziz Mohamad HMR

[1] Tiada perselisihan pada terma-terma perjanjian pinjaman berkaitan serahanhak oleh kerana serahanhak pada awal-awal lagi bukan sebahagian dari perjanjian. Persoalan s. 86 Akta adalah tidak berbangkit langsung. Jikapun perjanjian pinjaman mengandungi terma berkaitan serahanhak dan kemudian terma tersebut dibuang tanpa persetujuan perayu s. 86 masih juga tidak terpakai. Seksyen 86 tidak ditujukan untuk melaksanakan gadaian. Akibat dari s. 86 adalah untuk melepaskan jaminan bukan untuk menidaksahkan suatu gadaian.

[2] Di bawah s. 79 Akta, suatu jaminan di bawah satu kontrak gerenti bertujuan mengkotakan janji, atau melepaskan liabiliti pihak ketiga jika berlaku kemungkiran olehnya. Remedi bagi penerima gerenti adalah untuk mendakwa penjamin atas janjinya dalam kontrak gerenti jika pihak ketiga mungkir. Melalui gadaian, penggadai tidak menggerenti untuk mengkotakan janji atau melepaskan liabiliti pihak ketiga sekiranya dia mungkir. Remedi di bawah gadaian bukanlah terhadap tubuh badan si penggadai tetapi terhadap harta yang digadai, yakni remedi penjualan atau mengambil milik harta. Suatu gadaian bukanlah satu kontrak gerenti dan penggadai bukanlah seorang penjamin. Suatu gadaian adalah satu instrumen statutori, suatu cara dagang yang diizinkan oleh Kanun. Oleh itu, dalam kes semasa, jikapun terdapat perselisihan pada perjanjian pinjaman melalui pelepasan serahanhak, dan perselisihan itu dibuat tanpa persetujuan perayu, s. 86 tidak terpakai untuk menjadikan gadaian itu tak sah.

Rayuan ditolak.]

Case(s) referred to:

Co-operative Central Bank Ltd v. Y & W Development Sdn Bhd [1997] 4 CLJ 170 CA ***(refd)***

Legislation referred to:

Contracts Act 1950, ss. 79, 81, 86

National Land Code, ss. 253(1), 271(1), 340(1)

For the appellant - Ngeow Chow Ying; M/s CY Ngeow & Assoc

For the respondent - Trevor George De Silva (Mazura Kamaludin); M/s Shook Lin & Bok

[Appeal from High Court, Kuala Lumpur; Suit No: D3-22-653-1994]

Reported by Usha Thiagarajah

JUDGMENT

Abdul Aziz Mohamad JCA:

The appellant company had charged under the National Land Code a land of theirs to the respondents, a licensed finance company, as one of the securities for a loan given by the respondents to a company called Pembinaan Ikhlas-Jae Sdn Bhd ("the borrower"). The respondents subsequently sought to enforce the charge by applying to the land office for an order for sale. The appellants commenced an action in the High Court for a declaration that the charge was null and void, and for two orders that obviously were consequential orders, namely, an order stopping the enforcement action in the land office and an order that the title to the land be returned to the appellants. The judge dismissed the action and the appellants appealed to this court. We dismissed the appeal.

As far as the appeal was concerned, the facts that need be set out are these. By a letter of offer dated 1 August 1991, as amended on 29 August 1991, the respondents agreed to grant a loan of RM300,000 to the borrower. Among the securities specified in the letter of offer were a first fixed legal charge over 22 plots of land, one of which was the appellants' land, and an assignment from the borrower to the respondents of payments due to the borrower from a project that had been awarded to the borrower by MBf Construction Sdn. Bhd.

On 3 September 1991 a loan agreement was duly executed by the borrower and the respondents for a loan of RM250,000, not RM300,000. The loan agreement did not specify the assignment as one of the securities for the loan. On the same date, 3 September 1991, the appellants executed the charge over their land in favour of the respondents as security for the loan of RM250,000, not RM300,000. The charge was registered on 9 September 1991. By a letter dated 10 September 1991, the borrower sought from the respondents a waiver

of the assignment as a security on the ground that MBf Construction Sdn Bhd had refused their consent to the assignment. On 11 September 1991 the respondents replied agreeing to the deletion of the condition as to the assignment in the letter of offer and saying that the loan amount had been reduced from RM300,000 to RM250,000 "due to the insufficient security coverage". On 12 September 1991 the loan sum of RM250,000 was disbursed. It will be obvious from those facts that although the correspondence regarding waiver of the assignment and the consequential reduction of the loan to RM250,000 took place after the loan agreement and the charge were executed on 3 September 1991, when the loan agreement and the charge were executed on that date the waiver and the reduction had already been effected.

Practically the only question that arose in the appeal was whether the charge was null and void in consequence of the operation of s. 86 of the Contracts Act 1950, which provides as follows:

> Any variance, made without the surety's consent, in the terms of the contract between the principal debtor and the creditor, discharges the surety as to transactions subsequent to the variance.

If the section applies in this case, the "principal debtor" would be the borrower, the creditor would be the respondents and the surety would be the appellants. In the appeal, the stand taken by the appellants' counsel was that the contract for the purposes of s. 86 was the loan agreement of 3 September 1991. In submission in the High Court, the variance in the terms of the contract relied on by the appellants was the waiver of the assignment, although the variance specifically mentioned in the statement of claim was the reduction of the loan sum.

This was what the judge said on the question:

> To my mind the waiver of the assignment is not a variance that would entitle the plaintiff as a surety to be discharged from its liability. The assignment is another security which is independent of the charge executed by the plaintiff in favour of the defendant. The waiver of the assignment does not in any way alter the liability and obligations of the plaintiffs as nothing is stated in the annexure to the charge that this requirement is a term therein.

There seemed to have been some dispute in the High Court as to whether the appellants had consented to the alleged variance, because the judge said that the question was irrelevant in view of his finding that there was no variance.

To our mind there was no variance in the terms of the contract, that is the loan agreement of 3 September 1991, as regards the assignment, for the simple reason that, as has been seen, the term as to the assignment was never in the contract in the first place. The question of the application of s. 86 could not even begin to arise.

But even if the loan agreement had contained the term as to the assignment and subsequently the term was agreed to be removed without the consent of the appellants, to our mind section 86 would still not apply in this case. It is not intended to operate so as to affect a charge. The consequence of s. 86 is the discharge of the surety and not the invalidation of a charge. Section 79 of the Act provides, in its first part, as follows:

> A "contract of guarantee" is a contract to perform the promise, or discharge the liability, of a third person in case of his default. The person who gives the guarantee is called the "surety"; ...

For there to be a surety, therefore, there must be a contract of guarantee, in which the surety undertakes to perform the promise, or discharge the liability, of a third person in case of the third person's default. It is statutorily a three-party situation, although the third party is not a party to a contract of guarantee. Section 81 provides: "The liability of the surety is co-extensive with that of the principal debtor, unless it is otherwise provided by the contract", that is the contract of guarantee. The remedy of the person to whom the guarantee is given is therefore to sue the surety on his undertaking in the contract of guarantee if the third person defaults. The remedy is against the person of the surety. In the case of a charge, however, even a third-party charge, it is statutorily a bipartite situation between the chargor and the chargee. The default giving rise to remedies under the charge is always, statutorily, the default of the chargor, not of any third person. Thus s. 253(1) of the National Land Code speaks of the chargee obtaining the sale of the land charged "in the event of a breach by the chargor of any of the agreements on his part expressed or implied therein", that is, in the charge. And s. 271(1) speaks of the chargee's right to enter into possession of the land charged "at any time when the chargor is in breach of any agreement on his part expressed or implied in the charge". By the charge, therefore, the chargor does not guarantee "to perform the promise, or discharge the liability, of a third person in case of his default". And the remedy under the charge is not against the person of the chargor but against the property charged, that is the remedy of sale or taking possession of the property. Therefore a charge is not a contract of guarantee and the chargor is not a surety. According to *Co-operative Central Bank Ltd v. Y & W Development Sdn Bhd* [1997] 4 CLJ 170, a decision of this court,

a registered charge is not even a contract. Gopal Sri Ram JCA said at p. 173: "A registered charge is not a contract. It is a statutory instrument; a dealing; which the Code authorizes".

To conclude, even if there had been a variance of the loan agreement in this case by the waiver of the assignment and the variance was made without the appellants' consent, s. 86 did not apply to render the charge void in consequence.

The question of indefeasibility of title, which was argued in the High Court and in this appeal, would only arise should the appellants succeed in their s. 86 argument that the charge was void. The question that would have arisen then would be one of overcoming section 340(1) of the National Land Code, which gives indefeasibility to the title of the respondents to the land as a registered chargee. The appellants did not seek to argue that the respondents' title would not be indefeasible by virtue of any of the circumstances set out in sub-s. (2). They relied rather on sub-s. (4)(b) which provides: "Nothing in this section shall prejudice or prevent ... the determination of any title or interest by operation of law". The effect of the subsection is that indefeasibility of title cannot be set up to prevent the determination of a title by operation of law. The question that would have arisen under sub-s. (4)(b) would have been whether, the charge being void, there was determination of the title of the respondents "by operation of law". Would it be a case of determination of title by operation of law that is intended by that provision? As the appellants failed in their s. 86 argument, we did not think it was necessary to consider the question to determine the appeal and to dismiss it.